BEFORE

THE PUBLIC SERVICE COMMISSION OF

SOUTH CAROLINA

DOCKET NO. 2000-006-G - ORDER NO. 2000-875

NOVEMBER 9, 2000

IN RE: Annual Review of South Carolina Electric and Gas Company's Purchased Gas Adjustments and Gas Purchasing Policies.	))))	ORDER RULING ON PGA AND GAS PURCHASING PRACTICES

This matter comes before the Public Service Commission of South Carolina (the Commission) for the Annual Review of the Purchased Gas Adjustment (PGA) and the Gas Purchasing Policies of South Carolina Electric & Gas Company (SCE&G or the Company). In addition, pursuant to Order No. 94-1117, dated October 27, 1994, in Docket No. 94-008-G, the Commission considered the collection of environmental clean-up costs for the period under review.

By letter, the Commission's Executive Director instructed the Company to publish a prepared notice concerning the Annual Review of the PGA and the Gas Purchasing Policies, one time, in a newspaper of general circulation in the area affected by the review. The Notice indicated the nature of the review and advised all interested parties of the manner and time in which to file appropriate pleadings for participation in the proceeding. The Company was instructed to directly notify all of its customers affected by the review of the PGA. The Company submitted affidavits indicating that it had complied with these instructions. A Petition to Intervene was filed by the Consumer Advocate for the State of South Carolina (the Consumer Advocate). A hearing on the Annual Review was held on October 19, 2000, at

10:30 AM in the offices of the Commission with the Honorable William Saunders, Chairman, presiding. SCE&G was represented by Catherine D. Taylor, Esquire and Frank Mood, Esquire. The Consumer Advocate was represented by Elliott F. Elam, Jr., Esquire. The Commission Staff was represented by F. David Butler, General Counsel.

SCE&G presented the testimony of Julius A. Wright, W. Keller Kissam, John S. Beier, and Harry L. Scruggs (direct and rebuttal). The Consumer Advocate presented no testimony. The Commission Staff presented the testimony of Roy H. Barnette and Brent L. Sires.

Dr. Julius A. Wright testified on behalf of the Company. According to Dr. Wright, daily spot wellhead prices nationwide are nearly double the price of one year ago. Such an increase was not anticipated. Dr. Wright states that several factors have contributed to the recent extraordinary increase in natural gas prices. First, cutbacks in production by OPEC member nations resulted in rising oil prices this spring. As crude oil rose, so did natural gas prices. Second, demand has been growing, particularly in the area of gas-fired generation, while the production of natural gas has been declining over the past two to three years due to low natural gas prices during that period of time. This imbalance has put upward pressure on today's gas prices, and will continue to place upward pressure on prices for at least the next two years, according to Dr. Wright.

Dr. Wright opines that gas prices over the next one to three years will be dependent on a number of factors. Dr. Wright gave as an example the fact that current storage injection rates may not be sufficient to replenish storage for the upcoming winter, and current underground storage levels nationwide are about 18% below year-ago levels. If gas storage remains below prior year levels, this will put upward pressure on natural gas prices. Further, although drilling has picked up due to recent high prices, additional supplies are not expected to be available in quantities sufficient to lower gas prices in the first quarter of 2001, according to Dr. Wright. Dr. Wright noted additional factors that affect gas prices, such as storms in the Gulf of Mexico, a return to normal winter weather, and the amount of gas-fired electric generation being built or planned in this country. According to Dr. Wright, in general, the increasing demand for gas-fired generation, at least over the near term , should continue to put upward pressure on gas prices and keep supplies tighter than normally seen.

W. Keller Kissam, Vice President of Gas Operations for the Company also testified. Kissam testified as to the natural gas purchasing policies of SCE&G and the importance of the Industrial Sales Program (ISP). Kissam also offered testimony with regard to the Company's recovery of costs related to the environmental liability resulting from the cleanup of properties formerly used for manufactured gas plants (MGP).

Kissam noted that SCE&G contracts with South Carolina Pipeline Corporation (SCPC) for all of its natural gas supplies. Volumes are delivered from SCPC to SCE&G at 192 metered delivery points. Through Commission approved tariffs DS-1 and DISS-1, SCE&G has contracted with SCPC for a firm contract demand of 266,495 DTS per day. Kissam states that SCE&G relies on SCPC as its natural gas merchant for several reasons: 1) SCE&G does not own a pipeline system that connects SCE&G's 192 metered delivery points in its distribution system. The SCPC system provides this connection. 2)By serving SCE&G, and other customers, SCPC exerts significant market influence. Thus, according to Kissam, SCPC's market power is a benefit to SCE&G and its customers. 3) Operation of the SCPC system is backed by much experience, and SCPC has a thoroughly knowledgeable Staff.

Kissam testified that the Industrial Sales Program allows the Company to compete with alternate fuels in providing service to various interruptible customers. These customers could have switched to alternate fuels had it not been for the ISP program. According to Kissam, without these competitive sales, more fixed costs would be borne by the firm customers.

Kissam recommended no change in SCE&G's current Supply plan for 2000-2001, and states that the firm contract volume of 266,495 DTS remain in place for that timeframe.

Kissam states that SCE&G's purchasing practices were prudent, because they effectively balance reliability of supply and least cost. SCE&G's reliance on SCPC as a merchant affords SCE&G's customers reduced administrative costs while increasing its market power and system reliability in an energy market that changes daily. Further, the ISP program, according to Kissam, allows SCE&G to continue to retain interruptible load and reduce costs system-wide.

The environmental collection factor was also discussed by Kissam. SCE&G seeks no change in this factor from the present level.

The Company presented the testimony of John S. Beier, Supervisor of Gas Accounting and Regulatory for South Carolina Pipeline Corporation (SCPC). In Order No. 2000-590, Docket No. 1999-006-G, the Commission directed SCE&G, which is one of SCPC's sale-for-resale customers, to present testimony in this proceeding with regard to how SCE&G is benefited by SCPC's hedging program. Beier testified that he conducted SCPC's hedging program from its initial approval by the Commission in 1995 until December 1999. Further, as a part of his current duties, he states that he constantly reviews the results of the program and its effect on the weighted average cost of gas (WACOG) applicable to SCPC's firm customers. According to Beier, the hedging program helps to improve cost predictability for such customers as SCE&G, and reduces price risks associated with unexpected, radical cost changes that may occur over short periods in the gas spot market. Beier cautions that the hedging program cannot, however, remove all price volatility or eliminate the effect of changing gas prices.

Beier notes that, after a dramatic increase in natural gas prices, SCPC's hedging program does not currently indicate the purchase of either options or futures for the period including November 1, 2000 through October 31, 2001. However, Beier notes that since the inception of the hedging program through August 2000, SCE&G received a credit (subtraction from the cost of gas) of $2,354,152 as a result of SCPC's hedging activities. From September 1999 to August 2000, there was a subtraction from SCE&G's cost of gas of $4,166,535.

Harry L. Scruggs, Senior Rate and Regulatory Specialist in the Gas Rate Department of SCE&G testified as to the projected base cost of gas factor. Scruggs provided historical data for the review period September 1999 through July 2000, as well as providing computations for the projected cost of gas per therm for the future period November 2000 through October 2001.

With regard to the environmental cleanup cost factor, the Company is seeking recovery of the remaining balance of $20,704,439. SCE&G proposed that the factor remain at $.011 per therm as currently approved by the Commission.

With regard to the cost of gas, the current cost of gas is 68.835 cents per therm, approved by this Commission in Order No. 2000-590. The previous gas cost of 54.334 cents per therm was approved in Commission Order No. 1999-782, and was applicable the first billing cycle of November 1999.

Considering the cost of gas data for the historical period under review, the Company, according to Scruggs, has an actual over-collection of $2,008,494 as of August 31, 2000. The balance at October 31, 2000 is forecast to be an under-collection of $3,745,437, which was due to the rising prices for commodity gas.

As Scruggs states, the historic cost of gas is used as the starting point to project future gas costs. This cost is adjusted for known and measurable changes for the forecasted period November 1, 2000 through October 31, 2001. Much of the projection for the commodity cost of gas was affected by NYMEX index prices.

When all calculations are completed, SCE&G recommends a change in the cost of gas from 68.835 cents per therm to 78.151 cents per therm, an increase of 9.316 cents per therm. Scruggs notes that the end result, as projected, would have the Company experience an over-collection of $425 on its gas cost as of October 31, 2001.

Roy Barnette and Brent Sires of the Commission Staff testified. Barnette summarized the Audit Staff's findings, and stated that Staff had verified SCE&G's gas costs and Environmental Cleanup Costs for the twelve months ended August 2000. According to Barnette, SCE&G began the period with an under-collection of $1,275,216. The under-collection for the twelve months ended August 2000, including the projected months of September and October 2000 is $2,470,077. The cumulative under-collection is $3,745,293.

SCE&G's total environmental liability is $49,100,000. After deductions of $16,006,863 for amortization and collections, and $12,388,698 from insurance commitments, the outstanding balance is $20,704,439. Barnette also testified that SCE&G was correctly recovering its gas costs pursuant to its approved tariffs. See prefiled testimony and exhibits of Barnette.

Brent Sires also testified for the Commission Staff. Sires recounted the history of the gas cost recovery procedures approved by this Commission. Sires notes that a combination of historical data and projected data allows the Company to determine the appropriate base cost of gas. In the present case, the request for an increase in the proposed base cost of gas from 68.835 cents per therm to 78.151 cents per therm results in an increase of 9.316 cents per therm.

Sires notes that his observations of SCE&G's gas purchasing policies indicate that the Company receives adequate supplies of firm gas to meet its captive customers' needs. Sires reviewed the pipeline and propane-air supplies utilized by SCE&G. Sires pointed out that, based on SCPC's years of experience and expertise in pipeline operations, SCPC can adequately supply SCE&G with its present and future gas needs. Further, Sires concluded that SCE&G receives adequate supplies of firm gas to meet its captive customers' needs and is prudent with regard to its purchase of gas supplies from SCPC. Sires also noted that in light of the many changes which continue to take place which affect the securing and transportation of gas, the Company should continue its on-going program to ensure that its gas supply is consistent with its customers' needs and to ensure that supply efficiency is maintained at reasonable costs. Sires also opined that the operation of the Company's ISP program should continue, since this mechanism allows SCE&G to compete with alternate fuels.

Sires described SCE&G's pricing methodology for its emergency gas. Sires noted that SCE&G retains only the margin approved by the Commission for each unit sale of Emergency gas and credits the remainder to Cost of Gas. This past winter, the purchase price of gas escalated in parts of the country well above the current selling price of Emergency Gas of $8.75/dt. Because of this, according to Sires, the Company has modified its Emergency Gas Pricing methodology effective October, 2000 to determine a daily price based upon the posted daily Transco Zone 6 Non New York Price per dt. To this , the Company will add the approved customer Contract Markup with allowances for taxes and losses. The minimum price of emergency gas will continue to be $8.75/dt. Additionally, the Company has provisions in its General Terms and Conditions to Industrial Service Agreements for Gas addressing penalties for unauthorized Overrun of Gas by Firm and Interruptible customers.

The witness further stated that there is the potential for a sizable amount of Emergency Gas and Unauthorized Overrun Gas revenue to be collected from Industrial customers during a review period and the credit to Firm Cost of Gas from Emergency Gas during this review period was ($304,521). The revenue from Unauthorized Overrun Gas was $169,050, according to Sires, which is not currently being credited to Cost of Gas by SCE&G. Further, today, Sires notes that only the amount charged for Emergency Gas purchases above the allowed margin approved by the Commission is a credit to firm cost of gas. Staff's view is that there is the potential for additional natural gas cost to be incurred by the firm market when industrial customers utilize natural gas above the contracted Firm Maximum Daily Quantity or fail to discontinue utilizing natural gas on an interruptible basis after the Company calls for complete curtailment.

Staff, through witness Sires, made a recommendation addressing unauthorized overrun gas charges collected from industrial customers. Sires recommended that the Company's currently approved purchased gas adjustment tariff (PGA) be modified to include under the letter "D" of that PGA, the following language to be applied effective November 1, 2000:

> 4) The amount charged to Industrial Interruptible customers for Emergency gas purchases above the allowed Commission approved margin, and the amount charged to Firm and Interruptible Industrial customers for Unauthorized Overrun Gas purchases.

According to Sires, the impact of this recommendation will credit Cost of Gas amounts billed to Industrial customers resulting from Emergency Gas and Unauthorized Overrun Gas purchases.

Harry L. Scruggs also presented rebuttal testimony on behalf of the Company. Scruggs stated that he had no disagreement with Sires' recommendation, found at page 11 of his testimony, however, Scruggs wanted to provide some additional information and make clarifications concerning Emergency Gas (E-gas) and Unauthorized Overrun Gas. Scruggs noted that SCE&G developed an E-gas rate in February 1994 for interruptible customers during periods of curtailment. The Company wanted to have a mechanism in place that would allow customers to use natural gas for true emergency needs without adversely affecting firm gas cost or flow. Apparently, the use of E-gas is authorized only to forestall irreparable injury to life or property, including environmental emergencies. Thus, according to Scruggs, the Company does not believe that there is potential for a sizeable amount of emergency gas revenue. The original rate was set at $8.75 per dekatherm. The basis of the rate has been changed due to the increasing cost of gas, however, Scruggs states that the effects of the rate design remain the same. Scruggs states that margins to SCE&G have not been increased as a result of this mechanism and the firm cost of gas has always been, and will always continue to be credited with the non-margin proceeds.

Scruggs also stated that, for interruptible customers, unauthorized overrun gas, or penalty gas is gas taken by a customer after the effective hour of an order calling for their complete curtailment. For firm customers, according to Scruggs, it is gas taken by a customer without the Company's advance approval and which exceeds that customer's Maximum Daily Quantity (MDQ). Scruggs further states that there is not potential for sizeable amounts of revenue associated with penalty gas. If necessary, in case of deliberate disregard of curtailment orders, SCE&G is capable of cutting off the gas flow at the customer's location in order to stop the gas consumption. In addition, Scruggs states that SCE&G currently includes Penalty Gas revenue as a component in calculating a margin revenue requirement. Should this Commission approve Staff witness Sires' request, SCE&G would no longer do this since the Penalty Gas revenue would be included as a credit to the firm cost of gas. Scruggs noted that neither payment of an overrun penalty, nor purchase of emergency gas gives the buyers the right to take this gas.

FINDINGS AND CONCLUSIONS

Based on the evidence in the record, the Commission makes the following findings and conclusions:

1) The gas purchasing practices of SCE&G are prudent for the period under review, and SCE&G has properly recovered its gas cost pursuant to the terms and conditions of the Company's approved tariff.

The direct testimony of Company witness Kissam, and Staff witness Sires specifically support this conclusion.

Kissam notes that SCE&G purchases its gas from SCPC under tariffs approved by this Commission. By serving SCE&G and other customers, SCPC exerts significant market influence, and this market power may be used to benefit the acquisition of gas for SCE&G. Further, the operation of the SCPC system is backed by much experience among the various members of its knowledgeable Staff.

Staff witness Sires testified that SCE&G's gas purchasing policies provided adequate supplies of firm gas to meet its captive customers' needs at reasonable cost, and that he expected this to be true for the present and for the future.

2) The base cost of gas shall be 78.151 cents per therm effective and beginning with the first billing cycle in November 2000.

The direct testimony of SCE&G witness Scruggs supports this conclusion. Scruggs provided historical data for the review period September 1999 through July 2000, as well as provided computations for the projected cost of gas per therm for the future period November 2000 through October 2001. After all calculations are reviewed, the conclusion is that the base cost of gas should be increased to 78.151 cents per therm. (Scruggs at 6.) We regret this increase, but it appears that there is an inescapable conclusion that this figure represents the cost of gas for the next review period that comes closest to "zeroing out" the balance in the recovery of gas cost. Failure to institute this increase at this time would likely force the Company to under-recover their cost of gas. We would note that the Company's forecasts and models are quite sophisticated, and we are convinced that these are the best predictor of what gas costs will be in the future. We also note with interest the testimony of Dr. Julius Wright. There does not appear to be any relief in sight, at least for the near term, from the present trend toward higher gas prices. (Wright at 8-9.)

3) The Company shall continue to add a factor of $0.011 per therm in the PGA for environmental clean-up costs. This was virtually uncontested, and was discussed in the testimony of Company witnesses Scruggs and Kissam, and Commission Staff witness Barnette. (Scruggs Direct at 2-3; Kissam at 6-7; Barnette at 5-6.)

4) The current industrial sales program shall be continued. Again, this was virtually uncontested. The program was discussed in the testimony of Company witness Kissam and Staff witness Sires. (Kissam Direct at 4-5; Sires at 12-13.)

5) The Staff's recommendation to modify the Company's PGA effective November 1, 2000 to include under the letter "D" the amount charged to industrial interruptible customers for emergency gas purchases above the allowed Commission approved margin, and the amount charged to firm and interruptible industrial customers for unauthorized overrun gas purchases is hereby approved. We agree with Staff witness Sires that the impact of this recommendation will credit Cost of Gas amounts billed to Industrial customers resulting from Emergency Gas and Unauthorized Overrun Gas purchases. (Sires at 11-12.) We are mindful of the rebuttal testimony of Harry L. Scruggs, however, which states that revenues from such sources are limited in any case. We do note that Scruggs did not disagree with Sires' proposed procedure. (Scruggs Rebuttal at 1-2.)

6) The Consumer Advocate made three requests in this Docket: a) a finding by the Commission that SCE&G has not demonstrated economic prudence; b) a provision of the

Order requiring SCE&G to perform a detailed study and analysis of purchasing natural gas from suppliers other than South Carolina Pipeline Corporation; and (c) a provision of the Order requiring the establishment of a generic docket to examine the benefits and costs of offering all customers the ability to buy their supply service from marketers and their transportation service from SCE&G. We must deny each and every request of the Consumer Advocate.

First, as stated above, SCE&G has clearly demonstrated economic prudence. First, SCPC provides the pipeline that connects SCE&G's 192 metered delivery points in SCE&G's distribution system. Second, by serving SCE&G and other customers, SCPC exerts significant market influence. Thus, SCPC's market power is a benefit to SCE&G and its customers. Further, operation of the SCPC system is backed by a thoroughly knowledgeable staff, with years of experience. If SCE&G entered the gas purchasing market on its own, SCE&G would have to duplicate that staff, which would ultimately add an additional cost to the consumer. Finally, it should be noted that SCE&G buys its gas through Commission approved tariffs, which ensures that the prices SCE&G pays for its gas are just and reasonable. The Consumer Advocate's first request must be denied, in that SCE&G has demonstrated economic prudence in its gas purchasing practices. (See testimony of Company witness Kissam.)

Second, we deny the request to order a study of the alleged benefits of SCE&G's purchasing gas from suppliers other than SCPC. First, we reiterate the reasoning in the preceding paragraph as a partial basis for this denial. Second, as we stated in Order No. 1999-782, last year, such a study is inappropriate for a PGA proceeding, and such a study should be considered in an entirely new docket with all local distribution companies and other interested parties participating. We decline to order the study at this time, since we believe that the Consumer Advocate has not presented any evidence that this study is warranted.

Third, we deny the Consumer Advocate's request for the establishment of a generic docket to examine the benefits and costs of offering all customers the ability to buy their supply service from marketers and their transportation service from SCE&G. Again, we reiterate the reasoning stated above. In addition, we do not believe that the Consumer Advocate has presented any evidence to show that this study is warranted. We would request, however, that Staff continue to monitor the unbundling of natural gas supplies to Residential, Commercial, and Industrial customers in the State of Georgia, and, at a later date, make a recommendation to the Commission regarding the establishment of a generic docket addressing unbundling in South Carolina.

The tariffs and rate schedules shall be filed reflecting the findings herein within five (5) days of the receipt of this Order by the Company.

This Order shall remain in full force and effect until further Order of the Commission.

BY ORDER OF THE COMMISSION.

William Saunders

Chairman

ATTEST:

Gary E. Walsh

Executive Director

(SEAL)